

TRANSPORTATION

I. OVERVIEW

This Program Memorandum covers Transportation, the third of the eleven major programs in the statewide program structure.

The overall objective of the Transportation programs is to facilitate the rapid, safe, and economical movement of people, goods, and mail into, within, and out of the State by providing and operating transportation facilities and supporting services.

The Transportation program is composed of four principle sub-programs: Air Transportation Facilities and Services, Water Transportation Facilities and Services, Land Transportation Facilities and Services, and Overall Program Support for Transportation Facilities and Services. A total of 34 individual, lower-level programs and their associated plans are included in the Multi-Year Program and Financial Plan for the period 2007-2013.

The Department of Transportation is the only organizational entity involved in the Transportation program. Federal agencies involved include the: Federal Aviation Administration; Treasury Department; Department of Agriculture; Department of Commerce; Department of Health and Human Services; Department of Homeland Security; Department of Interior; U.S. Army Corps of Engineers; U.S. Coast Guard; Federal Highway Administration; Federal Transit Administration; Federal Maritime Commission; Transportation Security Administration; and the Environmental Protection Agency. In terms of financial assistance, the U.S. Department of Transportation is the most important of the federal agencies involved. Since county transportation systems must complement the State system, the County Planning Commissions and departments of planning and public works assist in determining the needs and priorities of transportation facilities. In addition, the City and County of Honolulu performs maintenance activities on all traffic lights on Oahu and removes abandoned vehicles from State highways.

The Department of Transportation plans, designs, constructs, operates, and maintains State facilities in all modes of transportation, including air, water, and land. Coordination with other State, County, and Federal programs is maintained in order to achieve the objective. The program currently provides, operates, and maintains eleven (11) commercial service airports, four (4) general aviation airports; nine (9) commercial harbors;

and two thousand four hundred twenty-three (2,423) lane miles of highway. Five major airports now serve domestic overseas carriers.

The Transportation program and its sub-programs are significantly affected by environmental concerns. Pollution controls, for example, increase operating and maintenance costs and can cause significant modifications, delays, or even cancellations of plans or projects. Changes in technology significantly affect the requirements needed in facilities, as do increases in volume requirements. The program strives to reduce its dependence on various energy resources. We are continuously reviewing conservation measures to reduce funding requirements and become more energy efficient.

The Transportation program is also affected by economic conditions. Recession and expansionary cycles affect air travel and in turn, tourist arrivals and cargo shipments. Fluctuations in the currency exchange rate also affect the number of overseas/passenger arrivals and the volume of imported and exported goods.

TABLE I-1

INVESTMENT AND OPERATING COSTS

TRANSPORTATION

	F i s c a l Y e a r s							
	Actual	Est.	Rec.	Rec.	P r o j e c t e d			
	<u>2005-06</u>	<u>2006-07</u>	<u>2007-08</u>	<u>2008-09</u>	<u>2009-10</u>	<u>2010-11</u>	<u>2011-12</u>	<u>2012-13</u>
A. <u>Costs of the Recommended Program</u> ^{A/}								
Capital Investment	405.7	934.2	512.9	202.6	630.3	126.5	279.0	...
Operating	552.9	617.3	632.4	611.4	611.8	611.3	613.2	613.8
Total	958.6	1,551.5	1,145.3	814.0	1,242.1	737.8	892.2	613.8

^{A/} Expenditures in millions of dollars from all funds.

II. COSTS AND EFFECTIVENESS OF THE RECOMMENDED PROGRAMS

AIR TRANSPORTATION FACILITIES AND SERVICES

The objective of the Level II program, Air Transportation Facilities and Services, is to develop, manage, and maintain a safe and efficient global air transportation organization with the spirit of aloha for Hawaii's residents and visitors. A total of 15 individual lowest-level programs and their associated plans are included in the Multi-Year Program and Financial Plan for the period 2007-2013.

The statewide airport system consists of eleven airports serving commercial airlines and general aviation flights, and four general aviation airports. Five of the major airports: Honolulu International Airport (HNL), Kahului Airport, Lihue Airport, Kona International Airport at Keahole and Hilo International Airport serve domestic overseas carriers.

Several non-State government agencies are involved in monitoring and controlling activities within the airport system. The Federal Aviation Administration (FAA) must certify that each airport serving scheduled air carriers properly conforms to applicable safety and security standards. The FAA provides air traffic control services for airports at Honolulu, Hilo, Kona, Kahului, Molokai, and Lihue. Since Honolulu, Kona, Lihue, and Kahului serve both domestic and international flights, the U.S. Immigration and Naturalization Service, Public Health Service, Department of Agriculture, the U.S. Customs and Border Patrol Service, and the U.S. Fish and Wildlife Service are involved in border clearance activities for travelers and cargo.

For passenger convenience, Hilo, Kona, Kahului, Lanai, and Lihue Airports have a Federal funded U.S. Department of Agriculture pre-departure program to inspect the baggage of passengers bound for the mainland who depart from these airports and interline or pass through Honolulu.

TABLE II-1

INVESTMENT AND OPERATING COSTS
AND
MEASURES OF EFFECTIVENESS/ACTIVITY

AIR TRANSPORTATION FACILITIES AND SERVICES

	F i s c a l Y e a r s							
	Actual 2005-06	Est. 2006-07	Rec. 2007-08	Rec. 2008-09	2009-10	P r o j e c t e d		
					2010-11	2011-12	2012-13	
A. <u>Costs of the Recommended Program^{A/}</u>								
Capital Investment	150.5	424.3	305.3	43.8	630.3	126.5	279.0	...
Operating	258.0	281.6	312.0	292.7	292.7	292.6	292.6	292.6
Total	408.5	705.9	617.3	336.5	923.0	419.1	571.6	292.6
B. <u>Selected Measures of Effectiveness/ Activity</u>								
<u>Honolulu International Airport</u>								
Avg. Time from Passengers Entering to Plane Take-off (Minutes)	150	150	150	150	150	150	150	150
Total Through-Put Cost (cents)	456	481	476	471	466	462	458	454
Passengers (000)	19,280	19,800	19,900	20,000	20,063	20,263	20,300	20,300
Cargo (000 tons)	361	365	368	372	376	380	384	388
Aircraft Operations (000)	209	300	300	305	310	310	320	320

^{A/} Expenditures in millions of dollars from all funds.

TABLE II-1 - Continued

	F i s c a l Y e a r s							
	Actual	Est.	Rec.	Rec.	P r o j e c t e d			
	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13
B. Selected Measures of Effectiveness/ Activity - Continued								
<u>Hilo International Airport</u>								
Avg. Time from Passengers Entering to Plane Take-off (Minutes)	90	90	90	90	90	90	90	90
Total Through-Put Cost (cents)	1,119	871	862	853	845	836	824	812
Passengers (000)	1,224	1,250	1,275	1,300	1,300	1,325	1,325	1,350
Cargo (000 Tons)	18	20	20	21	21	21	22	22
Aircraft Operations (000)	103	104	105	106	107	108	109	110
<u>Kahului Airport</u>								
Avg. Time from Passengers Entering to Plane Take-off (Minutes)	97	97	97	97	97	97	97	97
Total Through-Put Cost (cents)	288	246	243	241	238	236	234	232
Passengers (000)	6,863	6,000	6,000	6,500	6,500	6,500	7,000	7,000
Cargo (000 Tons)	52	33	33	34	34	35	36	36
Aircraft Operations (000)	157	160	162	165	166	167	167	169
<u>Lihue Airport</u>								
Avg. Time from Passengers Entering to Plane Take-off (Minutes)	85	85	85	85	85	85	85	97
Total Through-Put Cost (cents)	495	656	650	643	637	631	625	619
Passengers (000)	2,573	2,598	2,624	2,651	2,677	2,704	2,731	2,758
Cargo (000 Tons)	15,384	13,750	13,775	13,880	13,825	13,850	13,875	13,900
Aircraft Operations (000)	105	106	107	108	109	110	111	112

WATER TRANSPORTATION FACILITIES AND SERVICES

The objective of the Level II program, Water Transportation Facilities and Services, is to provide and effectively manage a commercial harbor system that facilitates the efficient movement of people and goods to, from, and between the Hawaiian Islands, and enhances and/or preserves economic prosperity and quality of life. A total of ten individual, lowest-level programs and their associated plans are included in the Multi-Year Programs and Financial Plan for the period 2007-2013.

The program consists of: (1) the improvement, operation, and maintenance of the statewide harbors system which consists of nine commercial harbors (Honolulu, Kalaeloa Barbers Point, Nawiliwili, Port Allen, Kahului, Kaunakakai, Kaunapali, Hilo, and Kawaihae) and (2) program leadership and staff support services, including planning, engineering and administration for the statewide harbors system. In accordance with Act 86, SLH 1990, the Hawaii Community Development Authority (HCDA) will assume full management and control of Kewalo Basin effective July 1, 2007 and Kewalo Basin will be removed from the statewide harbors system.

The primary activity within the statewide harbors system is the handling of containers, automobiles, equipment, bulk, neo-bulk, liquid, and general cargo. The cargo handling facilities are improved and maintained to meet the cargo volume. The growth of passenger ship activity and the need for berthing and terminal space, the proposed introduction of inter-island ferry operations in 2007, and the continued growth of cargo have also increased facility requirement demands.

Federal programs related to the Water Transportation Facilities and Services program include the programs of the U.S. Army Corps of Engineers, which administers and participates in the planning, construction, and maintenance of harbor navigational improvements. The Federal Maritime Commission regulates ports and marine terminal operators engaged in United States ocean borne commerce and receives and reviews tariff filings. The U.S. Coast Guard oversees maritime security at the commercial harbors and is also involved in the enforcement of safety and oil pollution regulations within harbor complexes of the State. The U.S. Treasury Department inspects foreign goods to insure a proper assessment of duty. Goods are also inspected by the U.S. Department of Agriculture to safeguard the State against the introduction of biological pests. The U.S. Customs and Border Patrol monitors the flow of foreign people and goods through state ports. The Environmental Protection Agency is involved with water quality standards.

TABLE II-2

INVESTMENT AND OPERATING COSTS
AND
MEASURES OF EFFECTIVENESS/ACTIVITY

WATER TRANSPORTATION FACILITIES AND SERVICES

	F i s c a l Y e a r s							
	Actual 2005-06	Est. 2006-07	Rec. 2007-08	Rec. 2008-09	2009-10	P r o j e c t e d		
						2010-11	2011-12	2012-13
A. <u>Costs of the Recommended Program^{A/}</u>								
Capital Investment	40.7	104.5	14.1	13.6	...	...	...	...
Operating	63.9	81.3	74.2	73.1	73.5	73.0	75.0	75.5
Total	104.6	185.8	88.3	86.7	73.5	73.0	75.0	75.5
B. <u>Selected Measures of Effectiveness/ Activity</u>								
<u>Honolulu Harbor</u>								
Program Cost Per Ton of Cargo (Water)	2.06	2.23	2.24	2.19	2.14	2.10	2.05	2.00
Total Cargo Tons Processed Per Acre Excl. Water Areas	36,933	37,746	38,576	39,425	40,292	41,219	42,167	43,137
Number of Passengers	703,474	950,608	998,716	1,030,748	1,032,809	1,034,875	1,036,945	1,039,019

A/ Expenditures in millions of dollars from all funds.

TABLE II-2 - Continued

	F i s c a l Y e a r s							
	Actual 2005-06	Est. 2006-07	Rec. 2007-08	Rec. 2008-09	2009-10	P r o j e c t e d		
					2010-11	2011-12	2012-13	
B. Selected Measures of Effectiveness/ Activity - Continued								
<u>Hilo Harbor</u>								
Program Cost Per Ton of Cargo	2.07	2.67	2.94	2.84	2.78	2.72	2.66	2.60
Total Cargo Tons Processed Per								
Acre Excl. Water Areas	40,561	35,657	36,441	37,243	38,063	38,938	39,534	40,750
Number of Passengers	500,962	607,304	655,412	687,444	688,819	690,197	691,577	692,960
<u>Kahului Harbor</u>								
Program Cost Per Ton of Cargo	1.08	1.26	1.54	1.45	1.41	1.38	1.35	1.32
Total Cargo Tons Processed Per								
Acre Excl. Water Areas	67,549	65,829	67,278	66,758	70,270	71,887	73,540	75,231
Number of Passengers	263,856	395,304	408,352	420,364	421,205	422,047	422,891	423,737
<u>Nawiliwili Harbor</u>								
Program Cost Per Ton of Cargo	2.33	3.04	3.65	3.48	3.41	3.33	3.26	3.18
Total Cargo Tons Processed Per								
Acre Excl. Water Areas	21,587	22,062	22,547	23,043	23,550	24,092	24,646	25,213
Number of Passengers	480,908	591,304	638,412	670,444	671,785	673,128	674,475	675,824

LAND TRANSPORTATION FACILITIES AND SERVICES

The objective of the Level II program, Land Transportation Facilities and Services, is to provide a safe and efficient highway system through the utilization of available resources and maintain, enhance, and support of land transportation facilities and programs. A total of eight lowest-level programs and their associated plans are included in the Multi-Year Program and Financial Plan for the period 2007-2013.

The program consists of the development, operation, maintenance, improvement, and administration of the statewide highway system consisting of approximately 2,423 lane miles of highway. Also included is the Safety Administration of Land Transportation program.

The Federal Government, through U.S. Department of Transportation's Federal Highway Administration (FHWA) and Federal Transit Administration (FTA), provides guidance and support to the state highway agencies in developing and operating their highway facilities. The State Highways Division initiates and administers state highway system projects. FHWA is responsible for reviewing and approving the amount and timing of Federal-aid funding for state highway projects. National Highway Traffic Safety Administration establishes and monitors highway safety standards while county planning and public works departments are involved in planning and programming various phases of highway construction for county highway projects. County police departments assist in enforcing traffic regulations.

Major activities include the delivery of the Capital Improvements Program projects, which averages \$120-170 million annually.

The Highways Division also provides significant support services for all four counties in processing County Federal-aid projects annually.

Operations of the State highway system consist of maintaining the statewide system of roads throughout the four counties with a staff of 1,025 positions. The major objective is to provide safe and reliable highway facilities for public use.

The Safe, Accountable, Efficient Transportation Equity Act: A Legacy for Users (SAFETEA-LU) authorizes the federal surface transportation programs for highways, highway safety, and transit for the 5-year period from 2005 to 2009. The new highway act provides federal funds of approximately \$160 million to \$170 million per year. Some of the federal highway funds that Hawaii receives are passed through to the counties and

other agencies. Federal highway funds used by the counties and other agencies vary and depend on the amount of projects they have programmed in the Statewide Transportation Improvement Program (STIP). The law requires that projects using Federal highway funds as well as those that are considered regionally significant be included in the STIP. However, the amount of funds that Congress allows the states to obligate each year (obligation limitation) is generally less than the funds apportioned. The obligation limitation has been approximately 90% of the apportionment.

TABLE II-3
 INVESTMENT AND OPERATING COSTS
 AND
 MEASURES OF EFFECTIVENESS/ACTIVITY
LAND TRANSPORTATION FACILITIES AND SERVICES

	F i s c a l Y e a r s							
	Actual 2005-06	Est. 2006-07	Rec. 2007-08	Rec. 2008-09	2009-10	P r o j e c t e d		
						2010-11	2011-12	2012-13
A. <u>Costs of the Recommended Program^{A/}</u>								
Capital Investment	214.6	405.4	193.5	145.2	...	...	...	...
Operating	205.1	224.3	216.0	211.2	216.2	216.2	216.2	216.2
Total	419.7	629.7	409.5	356.4	216.2	216.2	216.2	216.2
B. <u>Selected Measures of Effectiveness/ Activity</u>								
<u>Oahu Highways</u>								
Maint. Cost Per 10-Lane Miles (Dollars)	302,268	320,227	630,744	630,970	630,970	630,970	630,970	630,970
Roadway Maint. - Lane Miles	1,150	1,150	1,150	1,150	1,150	1,150	1,150	1,150
Landscape Maint. - Acres	2,254	2,254	2,254	2,254	2,254	2,254	2,254	2,254
Structure Maint. - Number	442	442	442	442	442	442	442	442

^{A/} Expenditures in millions of dollars from all funds.

TABLE II-3 - Continued

	F i s c a l Y e a r s							
	Actual 2005-06	Est. 2006-07	Rec. 2007-08	Rec. 2008-09	2009-10	P r o j e c t e d		
					2010-11	2011-12	2012-13	
B. <u>Selected Measures of Effectiveness/</u>								
<u>Activity - Continued</u>								
<u>Hawaii Highways</u>								
Maint. Cost Per 10-Lane Miles (Dollars)	106,468	124,226	143,981	144,046	144,046	144,046	144,046	144,046
Roadway Maint. - Lane Miles	774	774	774	774	774	774	774	774
Landscape Maint. - Acres	1,416	1,416	1,416	1,416	1,416	1,416	1,416	1,416
Structure Maint. - Number	133	133	133	133	133	133	133	133
<u>Maui Highways</u>								
Maint. Cost Per 10-Lane Miles (Dollars)	102,689	146,918	185,499	185,272	185,272	185,272	185,272	185,272
Roadway Maint. - Lane Miles	420	420	420	420	420	420	420	420
Landscape Maint. - Acres	260	260	260	260	260	260	260	260
Structure Maint. - Numbers	100	100	100	100	100	100	100	100
<u>Kauai Highways</u>								
Maint. Cost Per 10-Lane Miles (Dollars)	109,830	156,352	177,749	178,951	178,951	178,951	178,951	178,951
Roadway Maint. - Lane Miles	272	272	272	272	272	272	272	272
Landscape Maint. - Acres	719	719	719	719	719	719	719	719
Structure Maint. - Number	49	49	49	49	49	49	49	49

OVERALL PROGRAM SUPPORT FOR TRANSPORTATION FACILITIES AND SERVICES

The objective of the Level II program, Overall Program Support for Transportation Facilities and Services, is to enhance the effectiveness and efficiency of the Transportation Program by providing program leadership, staff support services, and general transportation related services.

The overall support program interacts with the Federal Transit Administration, U.S. Departments of Commerce, Defense, Interior, Transportation, Treasury, and U.S. Post Office. Close coordination of transportation facility planning with the counties is also maintained.

The FTA, under various programs, provides funding to states for the purpose of supporting public transportation. The assistance ranges from funding transit operations and facilities to assisting private nonprofit groups in meeting the needs of the elderly and persons with disabilities.

These programs interface with the Oahu Metropolitan Planning Organization as part of an overall comprehensive and coordinated planning process for all Oahu highway projects as well as airport and harbor projects.

The overall support program provides comprehensive transportation planning based on consideration of land use, socio-economic conditions, and environmental factors. Other ancillary services such as management, administrative support, internal control, and computer coordination are provided to the major transportation programs.

Financing for this program is provided on a pro-rata basis from the three special funds representing the three major activities of the Department of Transportation. These include the three other Level II programs of the Transportation major programs. The current pro-rata shares are as follow: Airport Revenue Fund - 44 percent; Highway Revenue Fund - 42 percent; and Harbor Revenue Fund - 14 percent.

TABLE II-4

INVESTMENT AND OPERATING COSTS

GENERAL ADMINISTRATION

	F i s c a l Y e a r s							
	Actual	Est.	Rec.	Rec.	P r o j e c t e d			
	<u>2005-06</u>	<u>2006-07</u>	<u>2007-08</u>	<u>2008-09</u>	<u>2009-10</u>	<u>2010-11</u>	<u>2011-12</u>	<u>2012-13</u>
A. <u>Costs of the Recommended Program^{A/}</u>								
Capital Investment	...	...	...	...	...	...	...	...
Operating	25.8	30.2	30.2	29.5	29.5	29.5	29.5	29.5
Total	25.8	30.2	30.2	29.5	29.5	29.5	29.5	29.5

A/ Expenditures in millions of dollars from all funds.

III. PROGRAM CHANGE RECOMMENDATIONS

AIRPORTS

Revenues for the Air Transportation Facilities and Services program are derived from concession fees, aviation fuel taxes, building space and land rentals, investment income, landing fees, airport use charges, federal grants, passenger facility charges and other sources. Committees comprised of representatives from the airlines and concessionaires act in an advisory capacity in reviewing airport operational plans and capital improvement program projects.

Operational and capital improvement program budgetary requests are prioritized based on health and safety, security, compliance with the FAA and environmental compliance, and maintenance of the facility. Rising fixed and capital costs are attributed to inflation and the airport modernization initiative. Increases in user fees such as landing fees and the Passenger Facility Charge will offset increases in these expenditures.

HARBORS

The Water Transportation Facilities and Services program is financed through revenues derived from wharfage, rentals, dockage, port entry fees, mooring charges, demurrage, cleaning, and other charges. Wharfage and rentals are the largest sources of revenue.

In the future, a tariff structure revision is programmed to ensure that sufficient revenue is generated to meet the bond compliance tests and maintain the financial health of the statewide harbors system. Wharfage tariffs have remained static since 1997 while capital improvement costs to maintain existing facilities and develop infrastructure and facilities to keep up with maritime demand as well as operating costs have grown. The continued development of the harbors system is dependent upon the financial ability to underwrite the capital improvement and operating costs. The Harbors Division continues to work on improvements to its business practices to gain improved sources of revenue and financial benefits. Effort is also underway to obtain federal funding assistance to address port security and major development initiatives needed to meet maritime infrastructure development needs.

HIGHWAYS

The Land Transportation Facilities and Services program is financed by the State motor fuel tax, rental motor vehicle and tour vehicle surcharge, State vehicle weight tax, State vehicle

registration fee, and Federal-aid funding for highway projects. The Capital Improvement Program is financed from highway revenue bonds, the highway special fund (cash), Federal-aid funds, general obligation bond funds, other funds (AMTRAK), and private contributions.

The Fiscal Biennium 2007-09 budget request reflects both the operating and capital improvement needs to sustain, maintain, and improve our State highway system based on priorities such as health & safety, compliance, emergency repairs, and enhancement. Act 263/91 authorized the rental motor vehicle tax and Act 223/99 established the tour vehicle surcharge tax. The current rates are as follows: motor vehicle rental, \$3.00 per day. Effective August 31, 2007, the tax reverts back to \$2.00 a day levied upon the lessor; tour vehicles 8-25 passengers, \$15.00 per month; and tour vehicles over 25 passengers, \$65.00 per month, levied upon the tour vehicle operator. The termination of the additional rate will have a financial impact to the program. The Division is thus considering various financial alternatives to address this issue in the upcoming Legislative Session.

IV. EMERGING CONDITIONS, TRENDS, AND ISSUES

AIRPORTS

A. Airline Lease Negotiations

Many of the airlines with flights to Hawaii are operating under the current terms and conditions of the existing airport-airline lease agreement. Each airline entering into this agreement is considered a signatory airline and the agreement governs the fees and charges payable to the State for use of airport facilities. There have been no active negotiations on a new lease for some time. While the State has a residual rate making methodology to set airline rates, the landing fees and system support charges have been held at present levels since the early 1990s. This has required the State to use the airport's cash reserves to make up the shortfall in airline revenue. The financial uncertainty of the airline industry following the September 11, 2001 terrorist attacks has further challenged the airport's ability to use its cash reserves to cover increased operating expenses and to meet coverage tests under the bond covenants.

B. Impact of September 11, 2001 - Aviation and Transportation Security Act

The tragic events of September 11, 2001 have permanently changed commercial aviation. As a result of the terrorist attacks, the FAA grounded commercial aircraft for three days and prevented foreign carriers from entering U.S. airspace for some time beyond that President Bush signed the Aviation and Transportation Security Act, which established the Transportation Security Administration (TSA). The TSA is responsible for overseeing the security of all modes of transportation, including aviation. Requirements of the Act include screening of all checked baggage, assuming airport security checkpoint responsibility from the airlines, and screening all checked baggage using an explosive detection system (EDS). TSA has funded additional screening equipment. The State, however, has had to fund infrastructure and other improvements to accommodate TSA's security screening operations.

The State of Hawaii had an insurance policy (DAGS - Risk Management) that insured against statewide economic losses suffered by state departments as a result of the actions of the Federal Government when they grounded all aircraft and reduced visitor flow into the State for several weeks. Department of Transportation Administration (DOTA) filed a claim in accordance with the insurance policy. DOTA and its insurance broker/consultant have invested a significant amount of time and effort in pursuing this claim. With the assistance of the Attorney General, supplemented by the expertise of consultants contracted by the Department of the Attorney General, we believe the outcome will be successful.

C. Concession Leases

Domestic passenger traffic has rebounded from the impacts of September 11, 2001. Airport concessionaires, some of whom experienced sizable drops in gross receipts immediately after September 11th, have seen sales rebound. In the most recently issued concession agreements, DOTA has included language that provides for periodic adjustments to the minimum annual guarantee (MAG) obligations and adjustments to percentage rents based on milestones. The language also allows for further MAG or rent adjustments in the event of an economic emergency similar to that caused by September 11th. Unlike domestic passenger traffic, international arrivals have declined recently due to a shortage of appropriately priced accommodations, reduction in number of available airline seats and competition from other destinations. The In-Bond concession, which suffered not only from the events of September 11th, but also from the SARS outbreak in Asia,

was re-issued in October 2003 with a reduced MAG, but with additional percentage rent required should certain sales milestones be reached. The concession rebounded from its lows following the outbreak of SARS, but the slow down in international traffic has slowed the concession's recovery as well. The re-issued contract was originally scheduled to expire on May 31, 2006, but was extended to May 31, 2007 under the concession agreement's holdover clause. The new major In-Bond location at Honolulu International was opened in January 2005 and DOTA felt the additional time would give potential bidders more data to use in reviewing the concession and deciding on a bid. The reduction in the current contract from previous contract levels will continue to impact Airports finances for some time.

D. Aviation Activities

For Calendar Year 2005, passenger traffic statewide increased by 5.2%, cargo increased by 0.7%, mail increased by 17.2%, and aircraft operations increased by 4.8% compared to Calendar Year 2004. At Honolulu International Airport, the passenger traffic increased by 4.2%, cargo increased by 2.8%, mail increased by 16.4% and aircraft operations increased by 3.1% when compared to the previous year. The statewide international passenger arrivals were also up by 2.3%.

E. Potential Capital Funding Sources

The Airport System Revenue Bonds, the Airport Improvement Program Discretionary Grants, and Passenger Facility Charges are several potential capital improvement program project funding sources that could be utilized by Airports Division.

Airports Division last issued Airport System Revenue Bonds for airport capital projects in 1991. The Division has managed its debt levels by issuing refunding bonds and defeasing bonds with unencumbered funds from the Airport Revenue Fund. Compared to other airport systems, the Airports Division has a relatively low amount of outstanding bond debt per enplaned passenger.

The FAA provides Airport Improvement Program Discretionary Grants for airport capital improvements. The amounts of discretionary grants are determined annually by congressional appropriation. Airport operators submit applications to fund specific projects with discretionary grants. These projects compete with projects submitted by other airport operators for the available amount of discretionary grants.

Since 1992, Passenger Facility Charges (PFC) has become an important source of funding for FAA approved airport capital projects throughout the country. Federal legislation allows the Airports Division to charge PFC only on overseas and international flights. The charging of PFC provides a significant funding source for airport capital projects. Effective October 1, 2004, the Division imposed a \$3.00 PFC for each overseas or international passenger boarding at Honolulu International Airport, Kahului Airport, Kona International Airport at Keahole, and Lihue Airport. In October 2008 of FY 2009, the PFC is scheduled to increase to \$4.50 to offset future capital costs. PFC revenues are applied on a pay-as-you-go basis to the greatest extent possible.

F. Environmental Concerns

Environmental requirements are increasing and ensuring compliance is becoming increasingly complex and costly. Fines, which can be issued for violations, can total in the millions of dollars. The Environmental Protection Agency (EPA) has conducted various inspections at airports statewide every year since 1999. Letters from EPA regarding findings of violations and orders to correct deficiencies observed during these inspections have been received. In 2005, the Airports Division, along with Highways and Harbors Divisions, incurred a Civil Penalty for violations to provisions of the Clean Water Act. The penalty was issued jointly by EPA and the State Department of Health's Clean Water Branch. A settlement of \$1,000,000 was reached with an explicit stipulation furnished in a Consent Decree that this amount did "not include any costs associated with corrective actions needed for compliance . . ." Additionally, a Supplemental Environmental Program was mandated, which involves the environmental auditing of baseyards at all airports with subsequent implementation of corrective actions based on the audit findings.

G. Modernization of the Airports

With air traffic rebounding from the September 11 terrorist attacks and the downturn in Japan's economy, the Governor's Economic Momentum Commission named the modernization of the State's airports, especially Honolulu International, as a key concern. In March of 2006, Governor Lingle and members of the Administration unveiled a \$2.3 billion, comprehensive 12-year Airports Modernization Plan as an effort to create a "world class" airport transportation system that meets the needs of our residents and visitors today and into the future.

The State's aging airport facilities are antiquated and need major improvement and renovation to its infrastructure that date back to the 1970s and earlier. These improvements include: greater passenger and baggage screening infrastructure that minimize congestion in the lobbies, projects that meet heightened security requirements at all checkpoints, the development of additional parking at all facilities, and other enhancements to comply with stringent FAA and EPA requirements such as on runway safety areas, surface water pollution, and perimeter security. The plan also addresses the new airline business model of direct overseas flights to neighbor island airports rather than the old model of hub-and spoke air transportation system.

These and other facility enhancements are being addressed in the current CIP and Special Maintenance Programs. The plan was developed in collaboration with the Airlines Committee of Hawaii and visitor industry partners based upon the diverse needs, financial feasibility, and with the goal of creating efficiencies and effectiveness in operations that increase the level of satisfaction for all residents and visitors.

HARBORS

A. Cruise Passenger Facilities

Hawaii's role in the cruise ship market continues to grow. Norwegian Cruise Lines (NCL) currently homeports three U.S. flagged cruise ships, the Pride of Aloha, the Pride of America and the Pride of Hawaii, providing the State with year round inter-island service. A foreign flagged ship, the Norwegian Sun, is planned to begin operations in 2007, replacing the Norwegian Wind as the fourth NCL vessel servicing Hawaii. Along with other cruise lines, the expected influx of visitors will have a positive impact upon the State's economy and increase the demand for additional berthing and comfortable and efficient passenger terminals throughout the limited commercial harbors area.

The Harbors Division has begun construction to lengthen Pier 3 in Hilo and Pier 3 at Nawiliwili Harbor. These improvements will offer vessel mooring capability for smaller sized cruise vessels. The Division has commenced the Kahului Harbor 2030 Master Plan update, a key aspect of which is the manner in which cruise service is addressed at the Kahului Harbor.

B. Ferry System

Inter-island passenger water borne transportation has historical roots in Hawaii's development. Hawaii Superferry,

Inc., a private ferry operator, will be introducing roll-on/roll-off high-speed daily inter-island ferry service for the transport of passengers and vehicles beginning July 2007 with a single vessel. The ferry is not intended to transport general commodities, containerized cargo or other cargo in bulk. Operations are planned between the harbors of Honolulu, Kahului and Nawiliwili. A second vessel is expected in the following 18-24 months to provide service between Honolulu and Kawaihae.

C. Cargo Facilities/Growth Issues

The continued growth in cargo has resulted in continuing increases in cargo operations. Matson Navigation Company continues to be the largest container operator servicing Hawaii with ships arriving at Honolulu Harbor three times a week. In October 2003, Matson implemented a new dedicated automobile roll-on/roll-off service every 14 days between Oakland, California and Honolulu and Kahului, Hawaii. Horizon Lines operates container ships between Honolulu Harbor and the west coast of the United States, with ships arriving at Honolulu Harbor twice a week, one of which proceeds on to the Far East. Young Brothers Limited operates inter-island vessels at Piers 39 and 40 in Honolulu Harbor and at most of the neighbor island harbors. In 2005, PASHA Hawaii Transport Lines LLC began providing auto delivery service through the use of the first modern pure car-truck carrier ever built in the United States. The ship is capable of carrying as much as 4,000 vehicles on ten decks. The introduction of the PASHA operation along with the need to accommodate cargo, ferry, and cruise line growth continues to place demand on the development of harbor expansion on all islands.

To address these demands, the Harbors Division has embarked on programs to provide additional operating areas on Oahu. In Honolulu, the Harbors Division began the development planning for the construction of a new container yard at the former Kapalama Military Reservation; completed design to remove a break bulk shed at Pier 1 to provide more operating room for foreign cargo deliveries, and is in the process of expanding operating areas for the Young Brothers Inter-island barge service. The Division was successful in re-acquiring the lands at Fort Armstrong that was previously transferred to the jurisdiction of the Hawaii Community Development Authority (HCDA). Undeveloped lands at the Kalaeloa Barbers Point Harbor are under negotiations to be privately developed to accommodate the installation of alternate fuel storage (ethanol and bio-diesel) facilities. These actions complement the State's energy efficiency and diversification effort. Along with these developments is work to establish a

delivery site for aggregate and sand for the cement industry due to the loss of local sources for the critical material needed to support our local construction industry.

Neighbor-island ports face similar growth challenges. Beginning in the fall of 2004, Matson began providing direct service to Kahului Harbor utilizing ocean-going ships. Matson also provides direct service to Hilo Harbor. Discussion is also underway with a woodchip operator who is interested in using Hilo Harbor to export eucalyptus woodchips to foreign markets. Due to limited pier and land facilities, the operator seeks to establish their chipping activity outside of the harbor on private lands with delivery onto ships only at the harbor. The Kahului Harbor Master Plan update is also underway and scheduled for completion in 2007. Included in the effort is the development of the west harbor coral stockpile site to enable expansion of the harbor. At the Kawaihae Harbor, repairs to damages sustained in the October 15, 2006 earthquake will need to be undertaken to assure the restoration of operational capability to serve the island of Hawaii. A second initiative will be the removal of the shed at Pier 2A and paving of an adjoining unpaved coral yard area planned to begin in 2007. This project will double the inter-island cargo handling capability at Kawaihae Harbor.

The U.S. Army Corps of Engineers continues to work on completion of the breakwater at the Kamaulupau Harbor on the island of Lanai. Damaged in Hurricane Iwa 24 years ago, the new breakwater is scheduled for completion in March 2007.

D. Environmental Concerns

The Harbors Division has been working with the State's Department of Health (DOH) and Principal Responsible Parties (PRPs) to address ground contamination within the Iwilei District at Honolulu Harbor. The U.S. EPA has monitored this effort.

Long-term mitigation measures may be required from the PRPs. Determining the appropriate level of remediation is on-going by the response activities of the PRPs. Through this effort, the PRPs are also undertaking and implementing long-term remediation measures that will assure the most effective and beneficial remediation of the contaminated areas.

Separate environmental improvement planning and training as part of a comprehensive effort by the State Department of Transportation is also being undertaken.

E. Seaport Security

The Harbors Division continues to upgrade security measures at all ports and seeks federal funding support for its security related manpower, infrastructure, and equipment needs to meet the substantial federal requirements imposed by the Maritime Transportation Security Act of 2002. Focus on the continuing effort is the development of improvements in staffing and facilities upgrades for access control. The Harbors Division anticipates having to implement new processing requirements associated with the issuance of the Transportation Worker Identification Cards (TWIC) and biometric access control systems that are being required under new federal legislation.

HIGHWAYS

A. Congestion

The Highways Division has undertaken numerous projects to alleviate traffic congestion throughout the State. In addition to increasing the capacity of our highways, we are also looking into ways of decreasing traffic demand by promoting ride sharing, flexible working hours, van pooling, car pooling, and the use of alternative modes, such as buses (both public and private), bicycling and walking through pedestrian-friendly facilities.

Numerous projects are currently being implemented to alleviate congestion along our most heavily traveled routes. On Oahu, the H-1 A.M. Zipper Lane extension and the Waimalu Viaduct widening have been completed and the Highways Division is proceeding with other congestion relief improvements such as the construction of North-South Road, H-1 P.M. Zipper Lane and widening of Fort Weaver Road. Neighbor island congestion relief improvements include the Lahaina Bypass project and widening of Piilani Highway on Maui; widening of Queen Kaahumanu Highway and Keaau-Pahoa Road on the Big Island; and the widening of Kaumualii Highway and Kuhio Highway on Kauai.

B. Safety

The Highways Division is developing a Strategic Highway Safety Plan (SHSP). The SHSP is a collaborative effort involving all safety stakeholders, and will identify statewide areas of safety concerns and develop countermeasures to reduce the number of serious and fatal traffic crashes.

Current safety programs include continuing implementation of intersection improvements, and installing/upgrading traffic signals, guardrails and drainage improvements. Safety analyses are conducted for all highway projects at the earliest stages of project development to ensure safety as a priority.

The Highways Division is actively pursuing driver behavior programs to improve safety on our highways. "Walk Wise Hawaii" for pedestrian safety, "Click It or Ticket" program for seat belt usage, and "52/12 - You Drink, You Drive, You Lose" for impaired driving are some of many ongoing safety programs by the Highways Division.

C. Environmental and Public Involvement

Hawaii has a unique and fragile environment, requiring stewardship in promoting, preserving, and enhancing the natural assets of the islands and striving to protect their beauty and sensitive areas. The development of highways facilities must be balanced against the need to protect the environment. The Highways Division continues to take a proactive approach in fulfilling its Federal Clean Water Act requirements.

Environmental assessment of our projects and mitigation of impacts is required prior to construction of our projects. The Highways Division will continue to hold informational meetings with community groups, seeking their input on current and future projects in their areas.

V. SELECTED PROBLEMS FOR POSSIBLE STUDY

AIRPORTS

The Airports Division is responsible for ensuring that its own facilities are in environmental compliance, together with those used by tenants (except for those tenants who have their own EPA permits). To do this, the Division's environmental program is being modified to have environmental health specialists at each of the four major airport districts, with central coordination being done on the administrative level. At each of the airports, the environmental health specialists will conduct inspections, help meet permit requirements, and monitor the various issues as required. At the administrative level, the following will be provided: (1) training in sampling and conducting inspections, (2) monitoring of existing and new

environmental regulations, (3) coordination of efforts with EPA and the State DOH, and (4) development and maintenance of an environmental database.

At HNL, a Small MS4 NPDES permit was issued, which greatly expands the amount of work and documentation needed to maintain the stormwater permit. For this and many other reasons, HNL has instituted a Web Based environmental asset management/task database to help fully understand the required tasks, regulatory requirements and documentation to maintain environmental compliance. Once fully implemented at HNL, it will be instituted at the 14 other airports.

HARBORS

Limited available land areas, financial constraints and the ability to implement major improvement projects continue to pose the greatest challenges to the Harbors Division. Focus is being placed on improvements in all three areas. As part of the effort, the Harbors Division has collaborated with the Hawaii Harbors User Group (HHUG) to coordinate the effort in identifying and focusing on the development of priority projects needed to improve the harbor program state-wide. A companion effort will be aimed at improving revenue to support and sustain improvement efforts through the revision of rentals and updating of the existing tariff structure. The pursuit of the development of new infrastructure through Public-Private development initiatives and the collaboration with the Department of Business, Economic Development and Tourism and the Aloha Tower Development Corporation as the development entity that will assist the Harbors Division on the expedited completion of major expansion projects is also being undertaken.

While the Harbors Division continues to develop expanded facilities to meet the cargo needs of the community at large, the Division has encountered specific community concerns to pier expansion at Kahului Harbor. In particular, there are conflicts between the need for continued harbor development to accommodate growth and the impact such expansion will have on ocean recreational use. Expansion and development of other ports may raise similar conflicts with recreational users that have in the past utilized non-developed commercial harbor properties and areas that are now required to meet harbor growth.

Sea transportation provides the State with the bulk of its imported goods and its primary means for exporting local products. The statewide harbors system must have the ability to support shipping and maritime commerce. This is a critical economic lifeline to the State. Harbor facilities are limited and as maritime needs increase, the challenge will be to

accommodate this growth is a critical area that must be addressed to assure the economic and social vitality of the State.

HIGHWAYS

The Highways Division has moved toward using various alternatives in lieu of building more highways. A Freeway Service Patrol project, which will utilize a series of roving tow trucks along Oahu's freeway system to assist in promptly handling minor freeway incidents, will begin operation in 2007. The Freeway Management System project will look at expanding our ability to identify incidents (with loops, CCTV cameras, and communication backbone) and timely communicate relevant commuter information to motorists.